

3-1-2021

Relational Contracting in International Commercial Trade

Kathryn St. John

Follow this and additional works at: <https://scholarlycommons.law.hofstra.edu/jibl>



Part of the [Law Commons](#)

Recommended Citation

St. John, Kathryn (2021) "Relational Contracting in International Commercial Trade," *Journal of International Business and Law*. Vol. 20: Iss. 2, Article 3.

Available at: <https://scholarlycommons.law.hofstra.edu/jibl/vol20/iss2/3>

This Article is brought to you for free and open access by Scholarship @ Hofstra Law. It has been accepted for inclusion in *Journal of International Business and Law* by an authorized editor of Scholarship @ Hofstra Law. For more information, please contact lawscholarlycommons@hofstra.edu.

RELATIONAL CONTRACTING IN INTERNATIONAL COMMERCIAL TRADE

By Kathryn St. John*

ABSTRACT

Recent free-trade agreement negotiations have raised concerns about the effect of free-trade agreements on sovereignty, democracy, and the rule of law. An often-repeated concern is that harmonization provisions, which seek to achieve regulatory equivalence, will jeopardize domestic standards. These concerns may be overcome through regulatory governance and cooperation. Mechanisms which seek to promote regulatory cooperation, such as the exchange of information following *ex ante* monitoring of goods, enable states to protect their own standards while positively influencing the regulations of their trading partners. Moreover, mechanisms promoting regulatory cooperation can enhance democracy since they require consultation and publication of information. These are examples of provisions contained within FTAs that resemble features of relational contracting. Incorporating these provisions in FTAs is advantageous to both parties and may help to overcome public opposition to FTAs.

I. INTRODUCTION

Free-trade agreements (“FTAs”) are met with resistance because of the public perception that FTAs undermine sovereignty, democracy, and the rule of law.¹ This resistance can be assuaged by incorporating regulatory governance and cooperative mechanisms that create a “space” in which states may protect their own regulations and standards.² Mechanisms that promote regulatory cooperation may enhance democracy since they promote balanced stakeholder input, increase transparency, and implement additional checks and balances.³ FTAs that utilize cooperative mechanisms resemble relational contracts because the inclusion of cooperative arrangements render the FTA “incomplete,” the future terms of which depend on the relationship between trading partners.⁴ Conceptualizing FTAs as relational contracts through the use of cooperative mechanisms will ultimately lead to economic benefits.

Democracy and sovereignty concerns relating to FTAs are well documented. FTAs—seen as the embodiment of globalization—are cast as the enemy of sovereignty.⁵ This has given rise to a perceived need to protect sovereignty and domestic laws against grants of authority to

* I am indebted to Dr. Oliver Gerstenberg of UCL Laws for his advice and feedback on an earlier version of this paper.

¹ Paul Magnette, *Wallonia Blocked a Harmful EU Trade Deal – But We Don’t Share Trump’s Dreams*, GUARDIAN (Nov. 14, 2016, 3:59 AM), <https://www.theguardian.com/commentisfree/2016/nov/14/wallonia-ceta-tip-eu-trade-belgium>.

² Ian R. Macneil, *The Many Futures of Contracts*, 47 S. CAL. L. REV. 691, 732 (1974).

³ *See id.* at 696.

⁴ *See id.* at 731.

⁵ Kyle Bagwell & Robert Staiger, *Domestic Policies, National Sovereignty, and International Economic Institutions*, 116 Q. J. ECON. 519, 519 (2001).

RELATIONAL CONTRACTING IN INTERNATIONAL COMMERCIAL TRADE

inter-governmental trade organizations.⁶ The perceived lack of democratic accountability of inter-governmental trade organizations has also prompted questions about their effectiveness and efficacy.⁷ Some authors, such as Bartl, further contend that membership of FTAs reduces the scope for domestic policy choices.⁸ The fundamental concern of critics is the need to protect domestic laws and standards from harmonization provisions since harmonization provisions that are designed to reduce regulatory differences can result in a race to the bottom.⁹ In response to this concern, Hoekman and Sabel argue that trade agreements that aim to achieve regulatory equivalence through cooperative mechanisms may achieve improved outcomes through mutual review and learning.¹⁰ This paper takes this rationale a step further and argues that these features of FTAs address sovereignty and democracy concerns, since they may be used to protect standards, and are also accommodating of potentially higher standards, such as protecting the scope of democratic choice.

Macneil and Macaulay developed relational (or essential) contract theory in response to perceived shortcomings with traditional “classical” contract theory.¹¹ Both scholars viewed “classical” contract theory as misconceived due to its characterization of contracts as discrete agreements.¹² They stated that contracts should be conceptualized as non-discreet agreements projecting future exchange and embedded in the relationship between parties.¹³ Relational contract theory is considered highly influential and widely accepted within the legal and management community for its insights.¹⁴ Macneil’s theory, however, has been criticized for its lack of tractability.¹⁵ Attempts have been made to develop more tractable models, but these do not deny the validity of Macneil’s premises.¹⁶ Therefore, Macneil’s relational contract theory will be used in this paper.

The literature also reveals the application of the relational contract theory in the context of FTAs as novel.¹⁷ However, there is a related, yet distinct, literature on “soft law” agreements, such as non-binding treaties and resolutions, which are non-binding agreements that contain normative provisions.¹⁸ Soft law agreements possess features typical of relational contracts (e.g., differing degrees of normative and relational intensity) and are arguably reliant

⁶ See Claude E. Barfield, *Free Trade, Sovereignty, Democracy: The Future of World Trade* 2 CHI. J. INT’L L. 403, 403 (2001).

⁷ *Id.*

⁸ See Marija Bartl, *Making Transnational Markets: The Institutional Politics Behind the TTIP*, EUR. & THE WORLD: A L. REV. 1, 15 (2017).

⁹ Ferdi De Ville & Gabriel Siles-Brügge, *Why TTIP is a Game-Changer and Its Critics Have a Point*, 24 J. EUR. PUB. POL’Y 1, 7 (2017).

¹⁰ See Bernard Hoekman & Charles Sabel, *Trade Agreements, Regulatory Sovereignty and Democratic Legitimacy*, 15 (Robert Schuman Ctr. for Advanced Stud., Working Paper No. 36, 2017).

¹¹ See Macneil, *supra* note 2, at 720. See generally Stewart Macaulay, *Non-Contractual Relations in Business: A Preliminary Study*, 28 AM. SOCIO. REV. 55, 60-61 (1963).

¹² Macneil, *supra* note 2, at 735. See generally Macaulay, *supra* note 11, at 64-65.

¹³ Macneil, *supra* note 2, at 747. See generally Macaulay, *supra* note 11, at 67.

¹⁴ Richard Austen-Baker, *Comprehensive Contract Theory: A Four-Norm Model of Contract Relations*, 2007 JCL LEXIS 45 *3 (2009).

¹⁵ *Id.* at *4.

¹⁶ *Id.*

¹⁷ See generally Henrik Horn et al., *Trade Agreements as Endogenously Incomplete Contracts*, 100 AM. ECON. REV. 394, 394 (2010) (stating that international trade agreements have been studied as incomplete contracts).

¹⁸ Teresa Fajardo, *Soft Law*, OXFORD BIBLIOGRAPHIES (Jan. 30, 2014), <https://www.oxfordbibliographies.com/view/document/obo-9780199796953/obo-9780199796953-0040.xml>.

on features of relational contracting for their interpretation (e.g., the assumption of reciprocity).¹⁹ However, they are not classified as relational contracts.²⁰ This paper bridges this gap. Section II discusses regulatory coherence and regulatory cooperation in FTAs. Section III applies Macneil's theory of relational contracting, including its underpinning assumptions, to FTAs. Section IV highlights the benefits of implementing the features of relational contracting into FTAs, which include an increase in flexibility to deal with evolving risks, an increase in regulatory coherence between states, and other economic benefits. Section V addresses criticisms concerning FTAs, including concerns that they undermine state sovereignty, democracy and the rule of law. This paper argues that these concerns may be addressed through the incorporation of features found in relational contracts.

II. REGULATORY GOVERNANCE AND COOPERATION

In recent decades, there has been an increase in the use of regulatory governance and cooperation in FTAs as a means to achieve regulatory coherence.²¹ Traditional FTAs were relatively rigid in their requirement to eliminate trade barriers.²² They permitted few exceptions, which often lacked teeth, exposing domestic public policy protections to legal challenge.²³ To address the limitations, subsequent agreements focused on procedural aspects.²⁴ This focus relied heavily upon principles of regulatory governance, such as broad stakeholder consultation and transparency.²⁵ Regulatory governance achieves regulatory coherence by ensuring states adhere to similar law-making processes.²⁶ At the same time, however, regulatory governance does not bind particular regulatory outcomes but, instead, respects the regulatory autonomy of states.²⁷

Regulatory cooperation also operates to achieve regulatory coherence. Broadly speaking, regulatory cooperation refers to the interaction between states facilitated through cooperative mechanisms.²⁸ It can take many forms, ranging from information sharing to equivalence arrangements.²⁹ Regulatory cooperation achieves regulatory coherence by enabling the identification of unnecessary regulatory differences and opportunities for joint

¹⁹ *Id.*

²⁰ *Id.*

²¹ William Kirst, *Trade Policy in Crisis*, WILSON CTR., <https://www.wilsoncenter.org/chapter-3-trade-agreements-and-economic-theory> (last visited Feb. 1, 2021).

²² *Id.*

²³ See General Agreement on Tariffs and Trade, Oct. 30, 1947, 61 Stat. A-11, 55 U.N.T.S. 194, at art. XX(b) [hereinafter GATT] (mentioning that it did not specify a procedure for resolving whether a measure was "necessary to protect human, animal, or plant life or health," which would otherwise be prohibited by the free trade provisions).

²⁴ See *infra* note 38 (explaining that the subsequent Agreement on the Application of Sanitary and Phytosanitary Measures [SPS Agreement] which entered into force in January of 1995 is comprehensive in detailing procedures for determining whether a procedure is prohibited).

²⁵ *Regulatory Coherence & Cooperation in the Transatlantic Trade and Investment Partnership (TTIP)*, U.S. CHAMBER COM. 5 (2015), https://www.uschamber.com/sites/default/files/regulatory_coherence_regulatory_cooperation_chamber_ttip_paper-final_2.pdf [hereinafter *Regulatory Coherence & Cooperation in the TTIP*].

²⁶ *Id.*

²⁷ *Id.* at 2.

²⁸ *Id.*

²⁹ *Id.*

RELATIONAL CONTRACTING IN INTERNATIONAL COMMERCIAL TRADE

promotion of relevant international standards.³⁰ There is also a perception that regulatory cooperation achieves more effective regulation in areas such as consumer protection, product safety, and the protection of plants and animals.³¹ For these reasons, global trading partners have increasingly utilized cooperative mechanisms.³² Also, plans were made to include cooperative mechanisms in recent proposed trade agreements, such as the Transatlantic Trade and Investment Partnership (“TTIP”).³³

Agreements on regulatory governance lay the foundation for regulatory cooperation in three ways. First, regulatory governance promotes interaction between states (i.e., by providing information on proposed regulatory acts and encouraging each party to consider the approaches of other parties), which fosters cooperation.³⁴ Second, regulatory governance means that states, through development of their own regulations, operate on similar information sets, which makes it easier to identify unnecessary divergence and opportunities for cooperation.³⁵ Third, adherence to the principles of regulatory governance, such as the publication of information, makes it easier for states to trust their counterparties; this facilitates regulatory cooperation because parties are more open to consultation with each other.³⁶

A. The Technical Barriers to Trade Agreement & the Agreement on the Application of Sanitary and Phytosanitary Measures

The Technical Barriers to Trade Agreement (“TBT Agreement”)³⁷ and the Agreement on the Application of Sanitary and Phytosanitary Measures (“SPS Agreement”)³⁸ were negotiated during the Uruguay round of negotiations on the General Agreement on Tariffs and Trade (“GATT”).³⁹ Both agreements entered into force with the establishment of the World Trade Organization (“WTO”) on January 1, 1995.⁴⁰ The TBT Agreement prohibits unjustified technical barriers that limit trade but does permit them for genuine public policy reasons, such

³⁰ *Good Regulatory Practices (GRPs) in TTIP: An Introduction to the EU’s Revised Proposal*, EUR. COMM’N 3 (Mar. 21, 2016), http://trade.ec.europa.eu/doclib/docs/2016/march/tradoc_154381.pdf [hereinafter *GRPs in TTIP*].

³¹ *Transatlantic Trade and Investment Partnership (TTIP) Chapter on Regulatory Cooperation: Detailed Explanation on the EU Proposal for a Chapter on Regulatory Cooperation*, EUR. COMM’N 4 (May 6, 2015), http://trade.ec.europa.eu/doclib/docs/2015/may/tradoc_153431.1.1%20Detail%20explanation%20of%20the%20EU%20proposal%20for%20a%20Chapter%20of%20reg%20coop.pdf [hereinafter *TTIP Chapter on Regulatory Cooperation*].

³² *Id.*

³³ See *infra* Section II B.

³⁴ *Regulatory Policy and the Road to Sustainable Growth*, OECD 9 (2010), <https://www.oecd.org/regreform/policyconference/46270065.pdf>.

³⁵ *Regulatory Coherence & Cooperation in the TTIP*, *supra* note 25, at 4.

³⁶ *GRPs in TTIP*, *supra* note 30, at 4.

³⁷ See Agreement on Technical Barriers to Trade, Apr. 15, 1994, 1868 U.N.T.S. 120 [hereinafter *TBT Agreement*].

³⁸ See Agreement on the Application of Sanitary and Phytosanitary Measures, Apr. 15, 1994, 1867 U.N.T.S. 493 [hereinafter *SPS Agreement*].

³⁹ *WTO Agreement on Technical Barriers to Trade*, INT’L TRADE ADMIN., <https://www.trade.gov/trade-guide-wto-tbt> (last visited Jan. 5, 2021) [hereinafter *WTO Agreement on TBT*]; *Understanding the WTO Agreement on Sanitary and Phytosanitary Measures*, WTO (May 1998), https://www.wto.org/english/tratop_e/sps_e/spsund_e.htm [hereinafter *Understanding the SPS Agreement*].

⁴⁰ *WTO Agreement on TBT*, *supra* note 39; *Understanding the SPS Agreement*, *supra* note 39.

as consumer protection.⁴¹ The SPS Agreement, on the other hand, is concerned with “all sanitary and phytosanitary measures which may directly or indirectly affect international trade.”⁴² These measures are ordinarily considered technical barriers to trade but, by virtue of the SPS Agreement, are subject to different disciplines.⁴³ The TBT Agreement and SPS Agreement do not merely target the removal of non-tariff barriers to trade, but they also aim to achieve regulatory harmonization through regulatory governance and cooperation.⁴⁴

1. Regulatory Governance

The TBT Agreement and SPS Agreement contain provisions that aim to achieve regulatory coherence through regulatory governance. The TBT Agreement provides the conformity assessment procedure, which includes procedures for sampling, testing and the inspection of products, with which products must comply before they can be placed on the market.⁴⁵ The SPS Agreement requires member states to consider certain scientific and technical factors, along with other risks, before permitting exceptions for particular products.⁴⁶ Article 2.4 of the TBT Agreement provides that, “[w]here technical regulations are required and relevant international standards exist or their completion is imminent, Members shall use them, or the relevant parts of them, as a basis for their technical regulations.”⁴⁷ The TBT Agreement contains similar provisions for standards and in relation to the conformity assessment procedure.⁴⁸ Meanwhile, the SPS Agreement promotes international standards and may accommodate member states’ regulatory autonomy. Under article 3, member states have the option to: (1) base measures on international standards, (2) conform measures to international standards, or (3) impose protections higher than international standards.⁴⁹

2. Regulatory Cooperation

The TBT Agreement and SPS Agreement also contain provisions that promote regulatory coherence through exchange and cooperation. For instance, article 7 of the SPS Agreement requires that members provide information to their trading partners concerning their SPS measures and must also notify them of any changes.⁵⁰ Article 11 of the TBT Agreement places an obligation on members to provide advice and technical assistance to other members (especially those from developing countries).⁵¹ Both agreements also create institutions to

⁴¹ See Ming Du, *What is a “Technical Regulation” in the TBT Agreement?*, 6 EUR. J. RISK REGUL. 396, 397 (2015).

⁴² SPS Agreement, *supra* note 38, at art. 1.1.

⁴³ See PETER VAN DEN BOSSCHE & WERNER ZDOUC, *THE LAW AND POLICY OF THE WORLD TRADE ORGANIZATION* 1185 (3d ed. 2013).

⁴⁴ *See id.* at 94; *Understanding the SPS Agreement*, *supra* note 39.

⁴⁵ TBT Agreement, *supra* note 37, at art. 5, 7-8.

⁴⁶ SPS Agreement, *supra* note 38, at art. 2.2, 5.2.

⁴⁷ TBT Agreement, *supra* note 37, at art. 2.4.

⁴⁸ *See id.* at annex 3L-O, art. 5.6-5.7, 5.9.

⁴⁹ SPS Agreement, *supra* note 38, at art. 3. However, this is subject to the risk assessment and management procedures in article 5.

⁵⁰ SPS Agreement, *supra* note 38, at art. 7.

⁵¹ TBT Agreement, *supra* note 37, at art. 11.

RELATIONAL CONTRACTING IN INTERNATIONAL COMMERCIAL TRADE

facilitate exchange.⁵² Additionally, the SPS Agreement establishes the “National Notification Authorities,” which are responsible for fulfilling notification requirements and responding to questions and requests for information from trading partners.⁵³

B. The Transatlantic Trade and Investment Partnership

The European Union (“EU”) and the United States (“US”) began negotiating the TTIP trade agreement in 2013.⁵⁴ The TTIP would have been the largest bilateral trade agreement ever negotiated between the world’s largest trading and investment partners.⁵⁵ In addition to market access rules, the TTIP encompassed rules on regulatory governance and cooperation.⁵⁶ In this respect, the TTIP would have created a template for potential future bilateral and multilateral agreements.⁵⁷ However, the TTIP was met with fierce opposition, particularly for undermining democracy and state sovereignty.⁵⁸ In 2016—in response to the criticisms—the new Washington Administration halted negotiations.⁵⁹ Although US trade officials later appeared receptive to reopening the door on trade negotiations, this door was firmly shut again.⁶⁰ Therefore, it is unclear whether the proposed rules on regulatory governance and cooperation will ever enter into force.

1. Good Regulatory Practices

The EU’s proposal for the TTIP sought to achieve consensus on regulatory governance as a means of achieving regulatory coherence.⁶¹ Specifically, in Chapter II of its proposal, the EU proposed a number of “Good Regulatory Practices” designed to “promote good governance in the regulatory process, in particular transparency, predictability and

⁵² See *id.* at art. 13; SPS Agreement, *supra* note 38, at art. 12. The TBT and SPS committees are effectively platforms for consultation.

⁵³ See SPS Agreement, *supra* note 38, at annex B (3-4). These measures do not bind outcomes and are consistent with state regulatory autonomy.

⁵⁴ Martin Nesbit et al., *Initiating a Public Dialogue on Environment Protection in the Context of the Transatlantic Trade and Investment Partnership (TTIP) Negotiations*, INST. FOR EUR. ENV’T POL’Y (Nov. 9, 2017, 10:55 AM), <https://ieep.eu/publications/initiating-a-public-dialogue-on-environment-protection-in-the-context-of-the-ttip-negotiations>.

⁵⁵ See Karel De Gucht, *Foreword*, in *THE POLITICS OF TRANSATLANTIC TRADE NEGOTIATIONS: TTIP IN A GLOBALIZED WORLD xvii* (Jean-Frédéric Morin et al. eds., 2015). The European Commission estimated that it would contribute €120bn and €90bn to the EU and US economies, respectively.

⁵⁶ See *State of Play of TTIP Negotiations Ahead of the 6th Round of the Negotiations*, EUR. COMM’N 2-5 (July 11, 2014), <https://www.tralac.org/images/docs/5913/ttip-state-of-play-11-july-2014.pdf>.

⁵⁷ See De Gucht, *supra* note 55, at xvii-xix.

⁵⁸ See *infra* Section V.

⁵⁹ Nesbit et al., *supra* note 54.

⁶⁰ Sam Morgan, *US Trade Chief “Open” to Resurrecting TTIP*, EURACTIV (June 1, 2017), <https://www.euractiv.com/section/economy-jobs/news/us-trade-chief-open-to-resurrecting-ttip/>; Emilie Bel, *Relaunching the Transatlantic Trade Agenda: A European Perspective*, ATLANTIC COUNCIL (Sept. 30, 2020), <https://www.atlanticcouncil.org/blogs/new-atlanticist/relaunching-the-transatlantic-trade-agenda-a-european-perspective/>.

⁶¹ See *TTIP – Initial Provisions for Chapter – Regulatory Cooperation*, EUR. COMM’N 2 (May 4, 2015), http://trade.ec.europa.eu/doclib/docs/2015/april/tradoc_153403.pdf [hereinafter *TTIP Initial Provisions*].

accountability.”⁶² The measures that relate to regulatory governance include obligations to: (1) publish information on domestic regulatory procedures and regulatory agendas,⁶³ and (2) provide opportunities for public consultation.⁶⁴ The measures that relate to the promotion of regulatory exchange include recommendations of: (1) the provision of information to one’s counterparty regarding new regulatory acts; (2) the consideration of one counterparty’s regulatory approach in undertaking a regulatory impact assessment; (3) the exchange of experience and information on retrospective evaluations.⁶⁵ By aligning domestic regulatory procedures and laying the foundations for regulatory cooperation, effective regulatory practices aim to achieve regulatory coherence.

2. Cooperative Mechanism

The EU’s proposal for the TTIP also intended to establish regulatory cooperation through procedures for exchange.⁶⁶ Article 11 of the proposal provides for the exchange of information on regulatory acts at a non-central level.⁶⁷ This highlights the voluntariness of the exchange.⁶⁸ Article 10 provides for regulatory cooperation at the central level, and, according to the EU, “provides a path for regulators to jointly assess appropriate means to promote compatibility.”⁶⁹ It specifically encourages states to engage with one another through review of conformity assessment procedures.⁷⁰ The goal of such early cooperation is to avoid the creation of unnecessary trade barriers before they are introduced.⁷¹

3. Regulatory Cooperative Body

Under the EU’s proposal, each party was to establish a Regulatory Cooperation Body (“RCB”).⁷² The purpose of the RCBs was to monitor the parties’ progress in, and to identify new opportunities for, regulatory cooperation.⁷³ The EU and the US intended law-making powers to remain with domestic regulators.⁷⁴ Instead, the RCBs were designed to provide a platform to engage EU and US regulatory authorities and high-level representatives of regulators.⁷⁵

⁶² *GRPs in TTIP*, *supra* note 30, at 2.

⁶³ *See TTIP Initial Provisions*, *supra* note 61, at 6-7, art. 5.

⁶⁴ *See id.* at 7, art. 6.

⁶⁵ *See id.* at 8, art. 7.

⁶⁶ *See id.* at 8-13, art. 8-13.

⁶⁷ *See id.* at 11, art. 11. Regulators determine whether any particular exchange takes place.

⁶⁸ *TTIP Chapter on Regulatory Cooperation*, *supra* note 31, at 7.

⁶⁹ *Id.* at 8.

⁷⁰ *See TTIP Initial Provisions*, *supra* note 61, at 10-11, art. 10.

⁷¹ *TTIP Chapter on Regulatory Cooperation*, *supra* note 31, at 9. It also promotes regulatory coherence without binding states to particular regulatory outcomes.

⁷² *See TTIP Initial Provisions*, *supra* note 61, at 12-14, art. 14.

⁷³ *See id.* at 13. RCBs were not to be vested with law-making power or to be a joint-decision making body.

⁷⁴ *TTIP Chapter on Regulatory Cooperation*, *supra* note 31, at 12; *Regulatory Coherence & Cooperation in the TTIP*, *supra* note 25, at 2.

⁷⁵ *TTIP Chapter on Regulatory Cooperation*, *supra* note 31, at 11.

RELATIONAL CONTRACTING IN INTERNATIONAL COMMERCIAL TRADE

III. INTERNATIONAL TRADE AGREEMENTS AS RELATIONAL CONTRACTS

Macneil's relational contract theory may be applied to FTAs. Relational contracts, as opposed to the "classic contract," do not contain all terms agreed upon, but, rather, depend on the relationship between the parties.⁷⁶ For example, consider long-term employment contracts.⁷⁷ In such contracts, the precise services employees will perform are not fully specified at the outset.⁷⁸ Instead, future services performed under the auspices of such contracts depend on social exchange (e.g., future negotiations).⁷⁹ This may also be the case with FTAs—whether bilateral or multilateral—that regulate trade barriers (e.g., tariffs and quotas) and outright prohibitions, since such agreements are not all encompassing.⁸⁰ For instance, during the TTIP negotiations, it was predicted that regulators would co-operate to develop new regulations and review existing regulations that impact the EU-US trade relationship.⁸¹ Future regulatory developments under the TTIP were not to be agreed at the outset, but, rather, determined in the future by balancing future advantages of increased similarity in regulatory requirements and reduced costs of compliance against contemporary domestic public interest concerns.⁸²

Additionally, FTAs fall within Macneil's characterization of exchange relationships: A contractual exchange relationship exists where parties have:

- an interdependent relationship which is dependent on reputation;
- varied individual and collective interests;
- priorities which are not measured (or monetized);
- shared responsibility for the allocation of risks;
- limited bindingness.⁸³

Parties to trade agreements have also established political and economic relationships.⁸⁴ In today's globalized world, it is clear that parties to trade agreements are often highly interdependent, especially due to the integration of global supply chains.⁸⁵ The

⁷⁶ See Macneil, *supra* note 2, at 721, 735.

⁷⁷ See *id.* at 705.

⁷⁸ See *id.* at 704.

⁷⁹ See *id.* at 705.

⁸⁰ Bohdan Kukharskyy & Michael Pflüger, *Relational Contracts and the Economic Well-Being of Nations*, IZA 1 (Dec. 2010), <http://ftp.iza.org/dp5394.pdf>.

⁸¹ *Regulatory Cooperation in TTIP*, EUR. COMM'N (2015), http://trade.ec.europa.eu/doclib/docs/2015/january/tradoc_153002.1%20RegCo.pdf.

⁸² *Id.*

⁸³ Ian R. Macneil, *Restatement (Second) of Contracts and Presentation*, 60 VA. L. REV. 589, 595 (1974).

⁸⁴ Giovanni Maggi & Andrés Rodríguez-Clare, *A Political-Economy Theory of Trade Agreements*, 97 AM. ECON. REV. 1374, 1378 (2007). Each economy's reputation is important since it impacts the willingness of other economies to enter into relations with it.

⁸⁵ *Interconnected Economies: Benefiting from Global Value Chains*, OECD 5 (May 28, 2013), <https://www.oecd.org/sti/ind/interconnected-economies-GVCs-synthesis.pdf>.

disruption of trade between countries may lead to a failure to produce domestic output.⁸⁶ While parties in negotiating agreements seek to promote their own interests, the negotiation and conclusion of trade agreements can advance collective interests by promoting overall welfare, especially between members of a customs union.⁸⁷ FTAs also frequently promote priorities, which are not measured or measurable in terms of monetary value.⁸⁸ For example, consider the EU customs union, which, through market integration and other measures, seeks to promote its broad objectives.⁸⁹ Meanwhile, parties to FTAs often share both the benefits and the burdens of the agreement.⁹⁰ For example, contingency arrangements, such as anti-dumping measures, protect domestic markets by levelling out prices between domestic and cheaper foreign goods.⁹¹ The economy importing the cheaper foreign product and the exporting economy share the burden of the potential disruption to the economy of the importing country.⁹²

The contractual terms of FTAs are also not fully binding.⁹³ Contemporary FTAs do not establish legally binding commitments in terms of tariff reductions.⁹⁴ Reduction commitments are, at least in the case of the WTO, included in non-binding goods schedules.⁹⁵ Such commitments, however, are not legally insignificant because they may be classified as “soft law,” since they are essentially normative.⁹⁶ In the international sphere, there is a significant incentive to comply with soft laws since compliance may influence an economy’s reputation and its relationships.⁹⁷ Implicit terms within these agreements potentially carry even less legal weight.⁹⁸ For instance, it can be assumed that when negotiating FTAs, the parties take one another’s process standards as given. They also presume that they will not be radically changed. This, however, does not give rise to a directly enforceable, legal commitment. Instead, compliance with this commitment depends on the relationship between the parties.⁹⁹

⁸⁶ Brett Johnson, *International Trade and Disruption of Supply Chains: Risk Management in the Pandemic Age*, JD SUPRA (Mar. 19, 2020), <https://www.jdsupra.com/legalnews/international-trade-and-disruption-of-58669/>.

⁸⁷ Arvind Panagariya, *Preferential Trade Liberalization: The Traditional Theory and New Developments*, 38 J. ECON. LITERATURE 287, 302-03 (2000).

⁸⁸ Alan B. Krueger, *Observations on International Labor Standards and Trade*, 3 (Nat’l Bureau of Econ. Rsch., Working Paper No. 5632, 1996).

⁸⁹ See generally Consolidated Version of the Treaty on the Functioning of the European Union art. 3, May 9, 2008, 2008 O.J. (C 115) 17 [hereinafter TFEU].

⁹⁰ Glen S. Fukushima, *United States-Japan Free Trade Area: A Skeptical View*, 22 CORNELL INT’L L.J. 455, 467 (1989).

⁹¹ Kimberly Amadeo, *Trade Dumping and Its Consequences*, BALANCE (Oct. 28, 2020), <https://www.thebalance.com/what-is-trade-dumping-3305835>.

⁹² *Id.*

⁹³ *Tariffs*, WTO, https://www.wto.org/english/tratop_e/tariffs_e/tariffs_e.htm (last visited Jan. 6, 2021).

⁹⁴ *Id.*

⁹⁵ *Id.*

⁹⁶ Gregory C. Shaffer & Mark A. Pollack, *Hard vs. Soft Law: Alternatives, Complements, and Antagonists in International Governance*, 94 MINN. L. REV. 706, 712 (2010).

⁹⁷ *Id.* at 713. This demonstrates the normative nature of soft law commitments.

⁹⁸ Dinah Shelton, *Commitment and Compliance: What Role for International Soft Law?*, CARNEGIE ENDOWMENT FOR INT’L PEACE (Nov. 22, 1999), <https://carnegieendowment.org/1999/11/22/commitment-and-compliance-what-role-for-international-soft-law-event-47>.

⁹⁹ However, as is the case with non-binding goods schedules, economies may still have significant incentive to comply with such commitments.

RELATIONAL CONTRACTING IN INTERNATIONAL COMMERCIAL TRADE

Relational contracting theory may also be applied to FTAs. According to Macneil, contracts fall along a continuum from highly relational to predominantly transactional.¹⁰⁰ For example, a long-term employment contract is a highly relational contract.¹⁰¹ A highly transactional contract, on the other hand, is one in which there is no precedent or future relations between the parties.¹⁰² Macneil identifies the purchase of gasoline at a petrol station as short and limited in scope.¹⁰³ FTAs may also be placed along such a continuum, suggesting that a relational contracting theory of FTAs has broad application. For instance, in recent years there has been a proliferation of regional trade agreements (“RTAs”), which aim to increase trade and economic growth through integration.¹⁰⁴ Examples include the proposed TTIP and Trans-Pacific Partnership (“TPP”), as well as the Regional Co-operation in Asia and the Pacific (“RCEP”).¹⁰⁵ Under these agreements, the level of integration aimed for is deeper than that in existing multilateral agreements.¹⁰⁶ As a result, RTAs are arguably more relational than existing multilateral agreements, since integrative mechanisms, such as regulatory co-operation, depend on the relationship between the parties.¹⁰⁷

IV. ADVANTAGES OF RELATIONAL CONTRACTING IN INTERNATIONAL TRADE AGREEMENTS

Features of relational contracting may be advantageous if incorporated into FTAs. FTAs may be easier to negotiate and easier to achieve state buy-in because FTAs do not specify all terms at the outset. Cooperative negotiations may also provide on-going flexibility, which can be used to protect local economies and to assist them in dealing with evolving risks, such as environmental harms and latent hazards. These advantages of relational contracting features support the usage of FTAs.

A. Economic Benefits of Relational Contracting

Should FTAs seek to constrain a wide range of behavior and provide for a variety of contingency situations, they will likely be more difficult to negotiate because more terms must be agreed upon. Moreover, states might be reluctant to join such restrictive agreements. On the other hand, if FTAs contain features of relational contracting (e.g., regulatory cooperation), which allow governments greater discretion in the future, negotiations will be simplified and could potentially increase states’ willingness to join such agreements. There is a positive relationship between the level of contract detail and negotiating costs because where a contract is more detailed, more must be agreed upon by the parties, which requires an increase in

¹⁰⁰ See Macneil, *supra* note 83, at 593.

¹⁰¹ See Macneil, *supra* note 2, at 704.

¹⁰² See *id.* at 720.

¹⁰³ See *id.* at 721.

¹⁰⁴ Iza Lejárraga, *Deep Provisions in Regional Trade Agreements: How Multilateral Friendly?*, OECD 4, 28 (Oct. 17, 2014), <https://pdfs.semanticscholar.org/1875/b78f17df1c6c9355bfb6b13b22b39efad85e.pdf>.

¹⁰⁵ *Id.* at 8, 35.

¹⁰⁶ *Id.* at 10.

¹⁰⁷ Thomas Bollyky, *The Role of Regulatory Cooperation in the Future of WTO*, RTA EXCH. 1-3 (June 2017), <https://e15initiative.org/wp-content/uploads/2015/09/RTA-Exchange-Regulatory-Coherence-Bollyky-Final.pdf>.

resources and time.¹⁰⁸ Therefore, it may be desirable to incorporate features of relational contracting into FTAs.

Discretion in FTAs could also protect local economies when there is economic uncertainty. In relational business contracts, high levels of flexibility are incorporated such that even key terms, such as the price of goods and terms of delivery, are determined in light of evolving economic and other factors.¹⁰⁹ This flexibility may be beneficial to parties because parties can negotiate the best outcome at the point at which the contract is to be delivered, ensuring that neither party is held to terms which are onerous or unfair. Likewise, in FTAs, flexibility may be introduced to achieve economic benefits. For instance, a party may introduce an escape-type clause, which opens tariffs up for renegotiation should there be a surge of imports following a sharp depreciation of the currency.¹¹⁰ An escape-type clause would protect industry from temporary, volatile economic conditions that could have disastrous consequences.

B. Relational Contracting Provides for Evolving Risks

Features of relational contracting in FTAs may also assist economies in dealing with evolving risks. This may be achieved through an understanding developed outside, or within, the terms of agreements or, alternatively, through regulatory cooperation. For instance, article 36 of the Treaty on the Functioning of the European Union does not explicitly list environmental protection as a ground on which to depart from the principle of freedom of the movement of goods.¹¹¹ Although the article 36 exceptions are exhaustive,¹¹² the Court of Justice of the European Union held that protection of the environment may constitute a mandatory requirement that permits departure from the freedom of the movement of goods, which causes additional concerns within the EU about environmental risks.¹¹³ Mechanisms that promote regulatory co-operation, such as through the exchange of information and expertise, may assist economies in dealing with evolving risks.¹¹⁴ Regulatory co-operation is identified as a means to deal with latent hazards in products that might not have been obvious at the point at which an agreement concluded.¹¹⁵ The exchange of information and expertise may help parties identify these hazards and determine how they should be effectively regulated.¹¹⁶

C. Relational Contracting Promotes Regulatory Coherence

Cooperative mechanisms, which provide for the sharing of information and negotiation in FTAs, may also help to bring about regulatory coherence. FTAs generally aim

¹⁰⁸ See Horn et al., *supra* note 17, at 395.

¹⁰⁹ See Jonathan Levin, *Relational Incentive Contracts*, 93 AM. ECON. REV. 835, 835 (2003).

¹¹⁰ See Horn et al., *supra* note 17, at 396.

¹¹¹ Charles Poncelet, *Free Movement of Goods and Environmental Protection in EU Law: A Troubled Relationship?*, 15 INT'L COM. REV. 171, 182 (2013).

¹¹² *Id.* at 181-83.

¹¹³ Case 302/86, *Comm'n of the European Communities v. Kingdom of Denmark*, 1988 E.C.R. 4627.

¹¹⁴ *Regulatory Cooperation in TTIP: An Introduction to the EU's Revised Proposal*, EUR. COMM'N 2 (Mar. 21, 2016), http://trade.ec.europa.eu/doclib/docs/2016/march/tradoc_154378.pdf.

¹¹⁵ See Hoekman & Sabel, *supra* note 10, at 4, 7, 15.

¹¹⁶ See *id.* at 6.

RELATIONAL CONTRACTING IN INTERNATIONAL COMMERCIAL TRADE

to reduce regulatory differences that might lead to trade distortions between countries.¹¹⁷ For instance, EU laws predicated on mutual and reciprocal recognition operate to harmonize regulations between Member States.¹¹⁸ Accordingly, if a product or service is compliant with domestic regulations, then it should be allowed to be traded in other Member States without being subject to additional or more onerous regulatory requirements.¹¹⁹ Regulatory cooperation, such as following *ex ante* goods monitoring, also operates to harmonize laws.¹²⁰ Through the exchange of information and expertise, trading partners can agree upon the appropriate regulation for a particular product or service.¹²¹

V. RELATIONAL CONTRACTING ADDRESSES CONCERNS ABOUT INTERNATIONAL TRADE AGREEMENTS

Features of relational contracts may also be incorporated into FTAs to address concerns that FTAs undermine sovereignty, democracy, and the rule of law. FTAs and multilateral trading organizations are often accused of undermining state sovereignty since grants of authority to multilateral trading organizations are alleged to undermine a state's ability to govern itself.¹²² Opponents also suspect FTAs of undermining democracy since, in addition to the view that FTAs limit democratic choices, industries may view FTA as secretive and controlling.¹²³ FTA dispute resolution processes, in particular, undermine the rule of law.¹²⁴ The use of relational contracting features in FTAs, however, may protect sovereignty as states retain discretion within a regulatory "space." Cooperative mechanisms within FTAs may also promote democracy by requiring consultation and the provision of information. Cooperative dispute resolution, which is open and relies on expert consultation, may address concerns about FTA dispute resolution and the rule of law.

A. Argument 1: International Trade Agreements Undermine Sovereignty

FTAs have often been criticized for undermining sovereignty of Member States because people are cautious of granting power to inter-governmental free trade authorities.¹²⁵

¹¹⁷ Gene Grossman et al., *The New Economics of Trade Agreements*, VOXEU (Sept. 23, 2019), <https://voxeu.org/article/new-economics-trade-agreements>.

¹¹⁸ See TFEU, *supra* note 89, at 22-23, art. 14 (providing for the harmonization of laws between EU Member States).

¹¹⁹ MICHAEL TREBILCOCK ET AL., *THE REGULATION OF INTERNATIONAL TRADE* 513 (4th ed. 2013).

¹²⁰ *Facilitating Trade Through Regulatory Cooperation*, OECD 8 (2019), https://www.wto.org/english/res_e/booksp_e/tbtsps19_e.pdf.

¹²¹ *Id.* at 93. For instance, one Member State may discover information on harms caused by a particular product which it might disseminate to its trading partners. The Member State, together with its trading partners, might subsequently agree on an appropriate standard for the regulation of that product, leading to appropriate, uniform regulation of that product in the states of the trading partners.

¹²² See Barfield, *supra* note 6, at 405.

¹²³ See Bartl, *supra* note 7, at 21; see also *Demand for the Democratisation of EU Trade Agreements*, MEHR DEMOKRATIE (Apr. 18, 2016), https://www.mehr-demokratie.de/fileadmin/pdf/Demand_for_the_democratisation_of_EU_trade_agreements.pdf.

¹²⁴ See J. H. H. Weiler, *The Rule of Lawyers and the Ethos of Diplomats: Reflections on the Internal and External Legitimacy of WTO Dispute Settlement*, (Harv. L. Sch., Working Paper No. 9, 2000).

¹²⁵ See Barfield, *supra* note 6, at 405-06.

Cooperative mechanisms and other relational contracting features of FTAs may be targeted with the same criticisms. The regulatory “space” created through cooperative mechanisms may still be viewed as a surrender of sovereignty. Such a view, however, is misguided as states retain control of this space. For instance, under the European chemicals regulation regime, which facilitates a harmonized system for chemicals trading within the EU, Member States create proposals using local knowledge and expertise and, further, consult stakeholders in the development of post-legislative guidance.¹²⁶ The burden then shifts to the EU to justify regulatory decisions in relation to particular substances.¹²⁷ Therefore, states, and not their inter-governmental authorities, would ultimately control the regulatory space created by cooperative mechanisms. Cooperative mechanisms should thus not be considered a significant concern for sovereignty and may in fact be included in FTAs to address sovereignty concerns.

A common sovereignty concern is that harmonization provisions within FTAs will lead to a lowering of standards.¹²⁸ Harmonization provisions aim to reduce distortions to trade by approximating regulatory standards, which leads to the elimination of stringent national laws.¹²⁹ Therefore, harmonization provisions are viewed as undermining state sovereignty as states with more stringent domestic protections lose power to determine their laws.¹³⁰ The same criticisms afflict regulatory governance and cooperation aimed at harmonizing laws.¹³¹ Negotiations could result in harmonization at standards less stringent than under more vigilant domestic regimes.¹³² The European Commission (“EC”), however, has been responsive to such concerns. For example, during the TTIP negotiations, the EC claimed that good regulatory governance practices would not undermine existing EU public policy protections.¹³³ However, the criticisms do not carry much weight. First, inter-governmental trade agreements often provide for minimum levels of approximation.¹³⁴ These are minimum standards for regulation that may be imposed even though states are left free to impose higher standards.¹³⁵ Secondly, under the “new” approach to regulatory harmonization, laws are harmonized according to general principles rather than detailed rules, which increases the scope for diversity in national laws.¹³⁶

Furthermore, the regulatory “space” that is created by cooperative mechanisms provides states with a means to protect or adopt regulations at a higher standard.¹³⁷ Provided states adhere to principles of regulatory governance and comply with procedures required by

¹²⁶ *REACH: Combining Harmonization and Dynamism in the Regulation of Chemicals*, in ENVIRONMENTAL PROTECTION: EUROPEAN LAW AND GOVERNANCE 56-57, 67-68 (Joanne Scott ed., 2009).

¹²⁷ *Id.*

¹²⁸ See De Ville & Siles-Brügge, *supra* note 9.

¹²⁹ See TFEU, *supra* note 89, at 22-23, art. 14.

¹³⁰ See Case 60/86, Commission of the European Communities v. United Kingdom of Great Britain and Northern Ireland, 1988 E.C.R. 3921 (discussing the reduced ability of lawmakers in the United Kingdom to introduce more stringent regulatory standards). The Court held that the United Kingdom could not mandate the manufacture of vehicles with dim-dip headlights.

¹³¹ See De Ville & Siles-Brügge, *supra* note 9, at 8.

¹³² See *id.* at 7-8.

¹³³ *TTIP Chapter on Regulatory Cooperation*, *supra* note 31, at 4.

¹³⁴ See Hoekman & Sabel, *supra* note 10, at 8-9.

¹³⁵ See *id.*

¹³⁶ See *id.* at 20.

¹³⁷ See *id.* at 9.

RELATIONAL CONTRACTING IN INTERNATIONAL COMMERCIAL TRADE

cooperative mechanisms, they can implement standards higher than international standards.¹³⁸ A Member State may discover information about a latent hazard in a product not known at the time the trade agreement is concluded and subsequently use this information to justify its reasons for adopting more stringent protections.¹³⁹ Therefore, cooperative mechanisms are tolerant of diversity. They can also be viewed as respecting state sovereignty, since states can protect their own standards where there is justification for higher levels of protection. Furthermore, states' input in determining international harmonized standards may be viewed as another manifestation of their sovereignty.

B. Argument 2: International Trade Agreements Undermine Democracy

FTAs are often criticized for unbalanced stakeholder input in their creation and have been viewed as controlled by the industry.¹⁴⁰ However, these allegations are not without foundation. Ninety-percent of EC consultations in the lead up to the TTIP negotiations were held with representatives from big businesses.¹⁴¹ This led 170 non-governmental organizations and institutions to condemn the TTIP negotiations as giving “unprecedented influence to business lobby groups to stop any new regulation that would impact trade and investment” leading to the “[prioritization of] trade and investment over the public interest.”¹⁴² They also viewed the negotiations as “a threat to democracy and an attempt to put the interests of big business before the protection of citizens, workers, and the environment” and as giving “enormous power to a small group of unelected officials to stop and weaken regulations and standards even before democratically elected bodies, such as parliaments, would have a say over them, thus undermining the democratic system.”¹⁴³ The stakeholder input problem is exacerbated by the secretive way in which FTA negotiations are conducted. In the TTIP negotiations, the US declined to release its proposals to the public.¹⁴⁴ Likewise, some EC proposals were withheld until there was significant public pressure, which ultimately denied the public an opportunity to meaningfully participate in the development of the regulations.¹⁴⁵

There is a potential risk that the industry might come to dominate the regulatory “space” created by cooperative mechanisms for a number of reasons. First, information used to regulate individual products is often dense and technical, requiring a level of expertise that the public does not have.¹⁴⁶ Second, citizens and NGOs may be excluded from the process of developing post-legislative regulatory guidance.¹⁴⁷ These concerns have been raised about the

¹³⁸ See *supra* Section II A 1 & 2.

¹³⁹ See generally Hoekman & Sabel, *supra* note 10, at 7.

¹⁴⁰ See *Demand for the Democratisation of EU Trade Agreements*, *supra* note 123.

¹⁴¹ See *id.*

¹⁴² *TTIP: Regulatory Cooperation is the Ultimate Tool to Prevent or Weaken Future Public Interest Standards for Citizens, Workers, Consumers, and the Environment*, CORP. EUR. (Feb. 2015), http://corporateurope.org/sites/default/files/statement_regulatory_cooperation_feb_2015_2.pdf.

¹⁴³ *Id.*

¹⁴⁴ See *Demand for the Democratisation of EU Trade Agreements*, *supra* note 123.

¹⁴⁵ See *id.*

¹⁴⁶ See Bartl, *supra* note 8, at 3; *Key Players*, EUROPA, https://ec.europa.eu/growth/sectors/chemicals/key-players_en (last visited Jan. 27, 2021); see also *id.*

¹⁴⁷ See *Key Players*, *supra* note 146. See generally Bartl, *supra* note 8, at 16-17.

REACH Guidance.¹⁴⁸ The Guidance determines through consultation the status of chemicals traded within the European Union.¹⁴⁹ Much of the REACH Guidance is dense and technical, which makes it difficult for the public to understand and to contribute.¹⁵⁰ Moreover, it is only in limited situations that the European Chemicals Agency engages in full public consultation and, even when it does, it engages with “Accredited Stakeholder Organizations”—dominated by powerful industry representatives—at the expense of public participation.¹⁵¹

Regulatory cooperation through cooperative mechanisms may also provide a defense to unbalanced stakeholder participation. Regulatory cooperation, when done properly, should involve publication of information and consultation with people from all sectors of the economy. Broader input should also result in better regulation because as a greater number of options have been considered. Moreover, the fact that FTAs, which involve regulatory cooperation, are essentially living agreements promotes opportunities for the public to participate. For instance, should the public uncover a hazard in a product, which only comes to light after the agreement has been concluded, and consequent to the use of the product, they could make submissions to influence the regulation of the product. Of course, due to the potential of the industry to control the negotiations under cooperative mechanisms, care must be taken to ensure that the public has adequate opportunity to participate.

Regulatory cooperation has also been regarded as undermining democracy by changing the way in which decisions are made.¹⁵² Bartl contends that regulatory cooperation, such as that proposed during the TTIP negotiations, has the potential to transform the EU regulatory culture.¹⁵³ She claims that US decision-making processes centered on a “neoclassical, welfare economics approach to cost benefit analysis” will dominate the regulatory “space” created by regulatory cooperation.¹⁵⁴ Bartl also contends that involvement of diplomatic and regulatory officials in discussions concerning scientific evidence will reinforce existing institutional biases.¹⁵⁵ Changes to decision-making for foreign institutional input, while simultaneously impacting the extent to which citizens and domestic legislators can have a say in the development of future regulations, gives rise to democratic concerns. Additionally, issues with oversight caused by institutional and sectoral control of the decision-making process, which challenges the democratic ideal because citizens and parliaments cannot effectively monitor and respond to regulatory developments.¹⁵⁶

Regulatory cooperation, however, does not pose the threat to democracy that Bartl suggests because there has been recognition on the part of international trade organizations to protect domestic decision-making processes. For example, in the context of the TTIP, the initial proposal for the RCBs sought to create “[a] streamlined procedure to amend the sectoral

¹⁴⁸ See generally *REACH*, EUR. COMM’N, https://ec.europa.eu/growth/sectors/chemicals/reach_en (last visited Jan. 22, 2021); *Key Players*, *supra* note 146.

¹⁴⁹ *Understanding REACH*, ECHA, <https://echa.europa.eu/regulations/reach/understanding-reach> (last visited Jan. 22, 2021).

¹⁵⁰ See generally *Guidance on REACH*, ECHA, <https://echa.europa.eu/guidance-documents/guidance-on-reach> (last visited Jan. 22, 2021).

¹⁵¹ *Stakeholders*, ECHA, <https://echa.europa.eu/about-us/partners-and-networks/stakeholders> (last visited Jan. 22, 2021).

¹⁵² See Bartl, *supra* note 8, at 3.

¹⁵³ See *id.* at 25.

¹⁵⁴ See *id.* at 33.

¹⁵⁵ See *id.* at 25.

¹⁵⁶ See *id.* at 36.

RELATIONAL CONTRACTING IN INTERNATIONAL COMMERCIAL TRADE

annexes of TTIP or to add new ones, through a simplified mechanism not entailing domestic ratifications procedures.”¹⁵⁷ In response to criticisms, however, a subsequent version of the proposal stated that “updates, modifications or additions will be adopted in accordance with the internal procedures of each party. The RCB will not have the power to adopt legal acts.”¹⁵⁸ Additionally, individual negotiations are not all one way. Although the US, for instance, might prefer to use cost benefit analysis in developing proposals for negotiations, its trading partners, such as the EU, might prefer to use more encompassing decision-making processes. The regulatory outcome agreed upon must be amenable to both parties. Moreover, as mentioned above, regulatory cooperation should increase transparency since stakeholder consultation requires the publication of information, and under cooperative mechanisms, the supply of information is continuous. This increased availability of information would likely result in an improvement in oversight.

FTAs are also regarded as constraining democracy by limiting citizens’ and parliaments’ legislative choices.¹⁵⁹ There is an underlying tension that FTAs are designed to promote consumer welfare, yet they place limits on consumers’ abilities to introduce laws that potentially constitute a barrier to trade.¹⁶⁰ In the context of the EU, environmental protection constitutes an exception to free trade provisions as a mandatory requirement.¹⁶¹ The free trade provisions contained within the TFEU, however, still restrict the implementation of measures that might obstruct trade since they must comply with additional requirements.¹⁶² According to Poncelet, the proportionality test has been a significant obstacle to the implementation of domestic protections.¹⁶³ There have been instances in which citizens have successfully lobbied governments to bring about regulatory change; however, private industries have attempted to sue the government due to the loss of profits from implementing such a trade barrier.¹⁶⁴ This conflict creates a constraint on democracy since both citizens and parliaments are likely to be wary of the consequences of their actions.

Measures seeking to achieve regulatory coherence through regulatory governance and cooperation are, in comparison to rigid harmonization provisions, respectful of democratic choices.¹⁶⁵ The EC, in its proposals for regulatory governance and cooperation, demonstrated a

¹⁵⁷ See *EU-US Transatlantic Trade and Investment Partnership: Trade Cross-Cutting Disciplines and Institutional Provisions*, EUR. COMM’N 5 (July 2013), http://trade.ec.europa.eu/doclib/docs/2013/july/tradoc_151622.pdf.

¹⁵⁸ *TTIP Initial Provisions*, *supra* note 61, at 13.

¹⁵⁹ See *Demand for the Democratisation of EU Trade Agreements*, *supra* note 123.

¹⁶⁰ See *Consumers at the Heart of Trade Policy: BEUC Position on the Future Trade and Investment Strategy*, EUR. CONSUMER ORG. 3 (June 22, 2015), http://trade.ec.europa.eu/doclib/docs/2015/october/tradoc_153849.pdf.

¹⁶¹ See Case 302/86, *Comm’n of the European Communities v. Kingdom of Denmark*, 1988 E.C.R. 4627.

¹⁶² See Case C-142/05, *Åklagaren v. Percy Mickelsson & Joakim Roos*, 2009 E.C.R. I-4304, I-4307.

¹⁶³ See Poncelet, *supra* note 111, at 184.

¹⁶⁴ See Daniel Hurst, *Australia Wins International Legal Battle with Philip Morris Over Plain Packaging*, *GUARDIAN* (Dec. 17, 2015, 9:19 PM), <https://www.theguardian.com/australia-news/2015/dec/18/australia-wins-international-legal-battle-with-philip-morris-over-plain-packaging>. Following the implementation of plain packaging laws in Australia, Phillip Morris attempted to sue the Australian Government under a Hong Kong-Australia bilateral investment treaty for appropriation of property. Although both cases were unsuccessful, they demonstrate that governments’ actions are not without implication.

¹⁶⁵ *Regulatory Coherence & Cooperation in the TTIP*, *supra* note 25, at 1-2.

willingness to respond to democratic concerns.¹⁶⁶ It emphasized that, under TTIP, “[w]e will keep our high levels of protection. In a number of areas, [the] EU and [the] US regulations provide similarly high levels of protection and could be compatible. In others, we will keep our different levels of protection.”¹⁶⁷ Further, the EC has stated that the “TTIP will reaffirm governments’ right to regulate to achieve legitimate public interest objectives.”¹⁶⁸ The EU’s regulatory governance and cooperation proposal requires adherence to additional obligations, but these are mainly procedural and consistent with good regulatory practice.¹⁶⁹ Under the TTIP’s cooperation provisions, specific regulatory outcomes are not binding.¹⁷⁰ Therefore, it is evident that regulatory governance and cooperation do not restrict democratic choice.¹⁷¹ Moreover, if pursuant to the negotiations, a state is provided higher levels of protection, or harmonization takes place at a higher level, it appears unlikely that the courts would strike down the negotiated regulations or let the private industry sue. Thus, the incorporation of cooperative mechanisms in FTAs may promote democracy through tolerance and increased legitimacy of protective standards.

Additionally, there are two ways in which regulatory governance and cooperation support democracy. First, institutions within the domestic government may inhibit democracy by restricting information and excluding citizens and public groups from the process of making laws; therefore, regulatory governance and cooperation typically require some degree of internal reorganization of domestic government.¹⁷² FTAs that contain reporting requirements as part of a deliberative process could help to overcome this because governments must establish oversight bodies in fulfillment of these requirements.¹⁷³ Second, the procedural requirements that are part of cooperative mechanisms are consistent with the “checks and balances” conception of democracy.¹⁷⁴ Mutual evaluation and monitoring by a state’s trading partners may promote democracy by ensuring that the state is adhering to the trading partners’ requirements. This mutual evaluation is similar to the function performed by constitutional courts and central banks at the national level.¹⁷⁵ A state’s trading partners may effectively perform this review function because they are not directly accountable to the people and not subject to the same political pressures (e.g., lobbying). The additional checks and balances they provide should ensure internal processes are functioning effectively and that they improve the overall quality of information and deliberation.¹⁷⁶ Essentially, mutual evaluation and monitoring can promote state democracy.

¹⁶⁶ See Ferdi De Ville, *Regulatory Cooperation in TTIP: A Risk for Democratic Policy Making?*, FOUND. FOR EUR. PROGRESSIVE STUD. 2-3 (Feb. 2016), https://www.feps-europe.eu/Assets/Publications/PostFiles/369_1.pdf.

¹⁶⁷ *Regulatory Cooperation in TTIP*, *supra* note 81.

¹⁶⁸ *Id.*

¹⁶⁹ *TTIP- EU Proposal for Chapter: Good Regulatory Practices*, EUR. COMM’N art. 1, 8 (Mar. 21, 2016), https://trade.ec.europa.eu/doclib/docs/2016/march/tradoc_154380.pdf.

¹⁷⁰ *Regulatory Coherence & Cooperation in the TTIP*, *supra* note 25, at 2.

¹⁷¹ De Ville, *supra* note 166, at 6.

¹⁷² See Robert O. Keohane et al., *Democracy-Enhancing Multilateralism* 18 (N.Y.U. IILJ Working Paper No. 4, 2007).

¹⁷³ *See id.*

¹⁷⁴ Thank you to Hannah Mminele for identifying independent oversight as consistent with the “checks and balances” conception of democracy.

¹⁷⁵ Keohane et al., *supra* note 172, at 7.

¹⁷⁶ *Id.* at 15.

RELATIONAL CONTRACTING IN INTERNATIONAL COMMERCIAL TRADE

C. Argument 3: International Trade Agreements Dispute Resolution Undermines the Rule of Law

Dispute resolution mechanisms within FTAs have received significant criticism due to their lack of transparency, which is a rule of law problem since dispute resolution processes and norms developed are neither prospective nor open.¹⁷⁷ Historically, problems between states were solved outside of the public eye using diplomatic power-based solutions.¹⁷⁸ The GATT initially made no provision for formal, juridical dispute settlement, with emphasis instead placed on cooperation and consensus.¹⁷⁹ However, there was a subsequent shift towards greater legalism with the introduction of panel procedures, which are used currently in the resolution of WTO disputes.¹⁸⁰ WTO dispute resolution at an internal level, however, is argued as not having changed much, as reflected in the attitudes of negotiators and internal settlement practices and procedures.¹⁸¹ This suggests that there are potentially on-going transparency and rule of law issues.

The mechanisms for dealing with investment treaty claims under FTAs have also been met with criticism for lack of transparency: For example, in the TTIP negotiations, EU governments and citizens were concerned about proposals for investor-state dispute settlements.¹⁸² Dispute resolution processes were portrayed as “secret” courts with trade disputes overseen by private industry lawyers who arbitrarily applied rules.¹⁸³ Furthermore, citizens were denied access to investor-state dispute settlements, which is a rule of law problem since it requires that people have recourse to the law.¹⁸⁴

A cooperative approach to dispute resolution, such as that found within relational business contracts, may be used to address rule of law criticisms of FTA dispute resolution. As outlined in Section II, in highly relational, long-term business contracts, not all terms that provide for future states of the world are specified at the outset.¹⁸⁵ This includes terms that detail how disputes are resolved, should they arise.¹⁸⁶ Instead, disputes are often resolved through negotiations between the parties that into consideration circumstances at the time of the dispute.¹⁸⁷ Such an approach, to the extent that it is not already used, could be incorporated into FTAs. There are, however, a number of specific features that should be incorporated to overcome rule of law problems. For instance, dispute resolution procedures should be open and

¹⁷⁷ See Weiler, *supra* note 124.

¹⁷⁸ TREBILCOCK ET AL., *supra* note 119, at 172.

¹⁷⁹ *Id.*

¹⁸⁰ Review of the Effectiveness of Trade Dispute Settlement Under the GATT and the Tokyo Round Agreements, Inv. No. 332-212, USITC PUB. 1793 (Dec. 1985) (Final), at 47.

¹⁸¹ See Weiler, *supra* note 124.

¹⁸² Peter H. Chase, *TTIP, Investor-State Dispute Settlement and the Rule of Law*, U.S. CHAMBER COM. (Dec. 2, 2015, 11:00 AM), <https://www.uschamber.com/issue-brief/ttip-investor-state-dispute-settlement-and-the-rule-law>.

¹⁸³ *Id.*

¹⁸⁴ Nathalie Bernasconi-Osterwalder, *Reply to the European Commission's Public Consultation on Investment Protection and Investor-to-State Dispute Settlement (ISDS) in the Transatlantic Trade and Investment Partnership Agreement (TTIP)*, INT'L INST. FOR SUSTAINABLE DEV. 16 (June 2014), https://www.iisd.org/system/files/publications/iisd_reply_eu_isds_ttip.pdf.

¹⁸⁵ See Macneil, *supra* note 2, at 761.

¹⁸⁶ *Id.* at 786.

¹⁸⁷ *Id.* at 787.

transparent to enable appropriate scrutiny of decisions.¹⁸⁸ Moreover, citizens and parliaments should not be denied participation in the development of norms through dispute resolution processes, even though such participation is likely to be indirect. One possibility would be to consider public interest views in reaching judgement.

The adoption of cooperative dispute resolution mechanisms within FTAs also addresses sovereignty concerns. Part of the concern about investor-state dispute settlement is that states are submitted to binding investment treaty arbitration.¹⁸⁹ Cooperative dispute resolution, which is open and transparent, would enable states to retain greater control of the process. States could, for instance, negotiate a resolution to their dispute, which is more mutually agreeable than the outcome of investment treaty arbitration. This would help address concerns that FTAs detract from sovereignty and also demonstrates that the inclusion of elements of relational contracting in FTAs can be positive.

VI. CONCLUSION

As mentioned, there has been an increased emphasis on regulatory governance and cooperation to obtain regulatory coherence in recent decades. Regulatory governance involves good regulatory practices, such as consultation with a range of stakeholders and transparency.¹⁹⁰ Regulatory cooperation, on the other hand, refers to the interaction between states through cooperative mechanisms, such as *ex ante* review.¹⁹¹ Regulatory governance and cooperation aspects of FTAs, therefore, can be compared to features of relational contracts.¹⁹²

Regulatory governance and cooperative mechanisms should be incorporated into FTAs to overcome concerns that FTAs undermine sovereignty, democracy, and the rule of law. FTAs have been accused of being the enemy of sovereignty due to the grant of authority they give to external trade organizations.¹⁹³ The closed nature of negotiations and dispute resolution has also led to accusations that they are contrary to democracy¹⁹⁴ and the rule of law.¹⁹⁵ Regulatory governance and cooperation provide a means to address these aforementioned concerns. They are consistent with sovereignty, since they allow states to pursue their own public policy objectives, while also not threatening domestic decision-making procedures. They also require public consultation and publication of information and transparency. To this end, regulatory governance and cooperation in FTAs overcome many of the concerns associated with traditional FTA agreements.

¹⁸⁸ See Weiler, *supra* note 124.

¹⁸⁹ *Demand for the Democratisation of EU Trade Agreements*, *supra* note 123.

¹⁹⁰ *Regulatory Coherence & Cooperation in the TTIP*, *supra* note 25, at 4.

¹⁹¹ *Id.*

¹⁹² *Id.* In particular, provisions providing for regulatory governance and cooperation in FTAs do not specify the final terms to be agreed upon. Such an analogy sheds light on the benefits of regulatory governance and cooperation, including economic benefits and management of evolving risks.

¹⁹³ See Barfield, *supra* note 6, at 407-08.

¹⁹⁴ *Demand for the Democratisation of EU Trade Agreements*, *supra* note 123.

¹⁹⁵ Weiler, *supra* note 124.